



Office of the Legislative Auditor

State of Montana

Report to the Legislature

December 1994

Financial-Compliance Audit For the Two Fiscal Years Ended June 30, 1994

State Auditor's Office

This report contains seven recommendations to the office related to:

- ▶ Electronic data processing controls.
- ▶ Recording estimated premium tax refunds payable in the General Fund of \$3,304,588 and \$4,428,941 at June 30, 1993 and 1994, respectively.
- ▶ Improving compliance with state laws and policies regarding:
 - ▶ Assignment of insurance company deposits.
 - ▶ Untimely deposits.
 - ▶ Unclassified positions.

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FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Office of the Legislative Auditor to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations which could have a significant financial impact. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

The Single Audit Act of 1984 and OMB Circular A-128 require the auditor to issue certain financial, internal control, and compliance reports regarding the state's federal financial assistance programs, including all findings of noncompliance and questioned costs. This individual agency audit report is not intended to comply with the Single Audit Act of 1984 or OMB Circular A-128 and is therefore not intended for distribution to federal grantor agencies. The Office of the Legislative Auditor issues a statewide biennial Single Audit Report which complies with the reporting requirements listed above. The Single Audit Report for the two fiscal years ended June 30, 1993 has been issued. Copies of the Single Audit Report can be obtained by contacting:

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Office of the Legislative Auditor

Financial-Compliance Audit

For the Two Fiscal Years Ended June 30, 1994

State Auditor's Office

Members of the audit staff involved in this audit were: Cindy S. Jorgenson, Wayne Kedish, Patti J. Robertson, and Kris Wilkinson.

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MARY BRYSON
Operations and EDP Audit

JAMES GILLET
Financial-Compliance Audit

JIM PELLEGRINI
Performance Audit

December 1994

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the financial activity of the State Auditor's Office for fiscal years 1992-93 and 1993-94. Issues discussed in this report relate to electronic data processing controls and accounting for premium tax refunds. In addition, we discuss noncompliance with state laws and policies governing timely deposits, position classification, assignment of insurance company deposits, and recording insurance examination costs. The office's written response to the audit recommendations is included in the back of the audit report.

We thank the State Auditor and his staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Scott A. Seacat", with a long horizontal flourish extending to the right.
Scott A. Seacat
Legislative Auditor

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Elected and Administrative Officials

State Auditor's Office

Mark O'Keefe

State Auditor

Dave Hunter

Deputy State Auditor

Frank Cote

Deputy Insurance Commissioner

Dave Hunter

Deputy Securities Commissioner

Tom Crosser

Administrator
Fiscal Management and Control

Summary of Recommendations

The listing below serves as a means of summarizing the recommendations contained in the report, the State Auditor's Office response thereto, and a reference to the supporting comments.

<u>Recommendation #1</u>	We recommend the office establish procedures to properly authorize, test, and document programming changes to facilitate recording revenue on SBAS in accordance with state accounting policy.	5
	<u>Agency Response:</u> Concur. See page B-3.	
<u>Recommendation #2</u>	We recommend the office establish procedures to estimate and annually record premium tax refunds payable.	7
	<u>Agency Response:</u> Concur. See page B-3.	
<u>Recommendation #3</u>	We recommend the office comply with section 33-2-606, MCA, by obtaining assignment of securities on deposit.	9
	<u>Agency Response:</u> Concur. See page B-4.	
<u>Recommendation #4</u>	We recommend the office establish mailroom procedures which ensure checks are deposited in accordance with state law.	11
	<u>Agency Response:</u> Concur. See page B-4.	
<u>Recommendation #5</u>	We recommend the office submit classification requests for unclassified positions in a timely manner.	12
	<u>Agency Response:</u> Concur. See page B-4.	
<u>Recommendation #6</u>	We recommend the office: A. Seek legislation to allow deposit of insurance examination revenues in the Special Revenue Fund, or	13
	<u>Agency Response:</u> Concur. See page B-4.	

Summary of Recommendations

B. Request General Fund budget authority
to spend insurance examination revenues. 13

Agency Response: Concur. See page B-4.

Recommendation #7

We recommend the office seek legislation
to clarify whether the Reinsurance Board
is a state program or a nonprofit nonstate
entity. 15

Agency Response: Concur. See page B-5.

Introduction

General

We performed a financial-compliance audit of the State Auditor's Office for fiscal years 1992-93 and 1993-94. The objectives of our audit were to:

1. Determine if the office complied with applicable laws and regulations.
2. Make recommendations for the improvement in administrative and accounting controls of the office.
3. Determine if the office's financial schedules present fairly the results of operations for the two fiscal years ended June 30, 1994.
4. Determine the implementation status of prior audit recommendations.

This report contains seven recommendations to the office. Other areas of concern deemed not to have a significant impact on the successful operations of the programs within the State Auditor's Office are not specifically included in the report, but have been discussed with management.

In accordance with section 5-13-307, MCA, we analyzed and disclosed the cost, if significant, of implementing the recommendations.

Office Background and Organization

The State Auditor's Office (office), established by Article VI, Section 1 of the Montana Constitution, has statutory responsibility to supervise the fiscal duties of the state and to keep an account of all state warrants.

The State Auditor is both the ex-officio Commissioner of Insurance and the ex-officio Commissioner of Securities. The State Auditor licenses and regulates insurance companies and agents within the state, and regulates and registers securities dealers.

Introduction

The office is organized as follows:

1. The Central Administration Division is responsible for the administrative, budgeting, personnel, and accounting functions of the office.
2. The Insurance Division regulates the insurance industry in Montana. Its duties include: resolving insurance consumer inquiries and complaints involving agents, coverage, and companies; licensing and reviewing the market and financial condition of insurance companies; collecting insurance premium tax; reviewing all rates and forms used by insurance companies; licensing, testing, and administering a continuing education program for all agents seeking to conduct insurance business in the state; and investigating insurance code and rule violations.
3. The Securities Division is responsible for the administration and enforcement of the Securities Act of Montana. The division is responsible for the registration of securities issuers, salesmen, investment advisers, broker-dealers, and investment adviser representatives. Additionally, it investigates instances of unregistered or fraudulent securities transactions.
4. The Fiscal Control and Management Division is responsible for issuing state warrants and collecting bad debts. The division processes and records all state warrants including duplicate, emergency, cancelled, and stale-dated warrants. The bad debt function collects and records bad debts owed to state and federal agencies.

The office is responsible for distributing a portion of insurance premium taxes to the Montana Public Employees' Retirement Division and to fire and police departments in qualifying Montana cities and towns. The office also distributes federal forest reserve moneys to Montana counties.

Prior Audit Recommendations

Prior Audit Recommendations

We performed the prior financial-compliance audit of the office for the two fiscal years ended June 30, 1992. The report contained eight recommendations to the office. During the current audit for the two fiscal years ended June 30, 1994, we determined the office implemented seven of the eight recommendations. The remaining recommendation, related to reviewing reports on examinations of insurance rating organizations, is no longer applicable due to changes in state law.

Findings and Recommendations

Accounting Issues

State law requires transactions entered on the state's accounting system be recorded in accordance with Generally Accepted Accounting Principles (GAAP). The Department of Administration, Accounting Bureau, has adopted state accounting policies which comply with GAAP. Accounting for financial activity in accordance with these requirements improves the quality, consistency, and comparability of the resulting financial information among agencies. It also ensures that revenue and expenditures are properly and consistently measured within each fiscal year.

Electronic Data Processing

The office uses a computerized revenue receipting system to classify securities, insurance, and bad debt revenues by type. Centralized services personnel enter each receipt in the receipting system and record total daily receipts as uncleared collections on the Statewide Budgeting and Accounting System (SBAS). Appropriate program personnel then access the receipting system and using the documentation submitted with the payment, classify each receipt according to type of revenue. Data processing personnel generate monthly reports which identify total revenues by type. Centralized services personnel use these reports to transfer uncleared collections into the appropriate revenue classification on SBAS.

In February 1994, data processing personnel completed an enhancement to an insurance data entry screen. Because office personnel gave maintaining system operations priority over maintaining system documentation, the programming changes made to complete this enhancement were not documented. Industry standards require all program changes be authorized, tested, and documented in order to maintain system integrity. The employee responsible for the enhancement terminated employment shortly after its completion. Due to the lack of documentation and turnover within the data processing unit, we were unable to determine whether the enhancement was authorized or tested prior to implementation.

The programming changes made for the enhancement inadvertently caused the revenue receipting program to improperly

Findings and Recommendations

classify the individual revenue receipts on the monthly summary reports. We determined \$359,684 was improperly classified on SBAS in fiscal year 1993-94. Table 1 summarizes the revenue misclassifications. In addition, we were unable to determine whether an additional \$124,592 was properly recorded as premium tax revenues on SBAS.

Table 1

General Fund Revenue Misclassification
Fiscal Year 1993-94

<u>Revenue Object</u>	<u>Revenue Class</u>	<u>Over(Under) Stated</u>
Insurance Licenses & Permits	Licenses & Permits	\$ 359,684
Premium Insurance Tax	Taxes	(317,433)
Fire Marshall Taxes	Taxes	(18,640)
Firemen's Pension Supplement	Taxes	(23,611)

Source: Compiled by the Office of the Legislative Auditor

Office personnel indicated they plan to rewrite the programming for the cash receipting system. They intend to address the identified errors when writing the new system. We believe the office can eliminate future revenue misstatements by establishing procedures to ensure all system enhancements are properly authorized, tested, and documented prior to implementation.

Recommendation #1

We recommend the office establish procedures to properly authorize, test, and document programming changes to facilitate recording revenue on SBAS in accordance with state accounting policy.

Findings and Recommendations

Premium Tax Refund Payable

The office assesses and collects a tax on premiums written by insurance companies conducting business in the state of Montana. Premium tax collections were \$28,017,371 and \$27,115,410 in Fiscal Years 1992-93 and 1993-94, respectively.

Beginning in 1988, the office required insurance companies subject to the tax to submit quarterly estimated payments. Previously, companies paid the entire tax amount with their required annual filing. The estimated payments and resulting tax assessment are calculated based on premiums written during a calendar year. Once companies began submitting estimated tax payments, the amount of taxes remitted began exceeding the total tax assessed at the time of the annual filing each March. By March 1994, insurance companies had accumulated a total credit balance of approximately \$3,900,000. In fiscal year 1991-92, office personnel implemented procedures to notify insurance companies regarding the credit balances. In an effort to reduce the total credit balance, the office now issues refunds when a company accumulates a significant balance. Refunds are also made if requested by the company. The office requested us to determine whether the credit balance and related premium tax revenues were properly recorded as required by state accounting policy.

We determined the office did not record a liability on SBAS for the outstanding credit balance. In addition, the office has not established procedures to identify potential refunds related to the estimated payments received prior to the end of each fiscal year for the next calendar year's tax assessment. For revenues subject to refund, such as the premium tax, state accounting policy requires the office to record an estimated liability and corresponding reduction in revenues for anticipated refunds.

We analyzed available documentation and estimated unrecorded refunds payable in the General Fund of \$3,304,588 and \$4,428,941 at June 30, 1993 and 1994, respectively. Table 2 outlines the misstatement to the State's General Fund and the office's schedule of changes in fund balance for the two fiscal years ended June 30, 1994.

Findings and Recommendations

Table 2

Premium Tax Misstatement

	<u>Over(Under) Stated</u>	
	<u>Fiscal Year</u> 1992-93	<u>Fiscal Year</u> 1993-94
<u>Statewide General Fund</u>		
Accounts Payable	\$(3,304,588)	\$(4,428,941)
Revenue	(228,184)	1,935,743
Prior Year Revenue	(511,872)	(811,390)
Beginning Fund Balance	4,044,644	3,304,588
Ending Fund Balance	3,304,588	4,428,941
<u>Schedule of Changes in Fund Balance</u>		
Revenue	(228,184)	1,935,743
Prior Year Revenue	(511,872)	(811,390)
Support to State of MT	(740,056)	1,124,353

Source: Compiled by the Office of the Legislative Auditor

The office should establish procedures to annually estimate the amount of anticipated refunds payable related to premium tax revenues and record that estimate on SBAS in accordance with state accounting policy.

Recommendation #2

We recommend the office establish procedures to estimate and annually record premium tax refunds payable.

State Compliance

We reviewed selected state laws and regulations pertaining to the office. The following sections discuss state compliance issues we noted during the audit.

Assignment of Insurance Company Deposits

In accordance with section 33-2-111, MCA, the office requires insurance companies writing insurance policies in the state of Montana to place in trust a deposit of cash or securities for the protection of policyholders. Insurance division personnel determine each company's required deposit amount based on criteria

Findings and Recommendations

outlined in state law. Insurance company deposits currently amount to \$11.2 million. Of this, \$4.2 million is from Montana based (domestic) insurance companies. The remaining \$7 million is from insurance companies based outside of Montana (foreign). In the event a company becomes insolvent, the State Auditor is responsible for liquidating the related deposit for use in protecting the financial interests of the policyholders.

Section 33-2-606, MCA, requires the deposits be assigned to the State Auditor if the securities are not negotiable by delivery. A security negotiable by delivery is one for which ownership transfers based on possession. Based on our review of supporting documentation, none of the securities held in trust are assigned to the State Auditor. Office personnel were unable to provide documentation as to whether the securities on deposit are negotiable by delivery.

As a result of not requiring insurance company deposits be assigned, the office is in noncompliance with section 33-2-606, MCA. If the securities are non-negotiable, the commissioner cannot use them unless and until they are legally transferred to the commissioner. The purpose of assignment is to give the commissioner immediate access to the deposits if necessary to pay policyholders. By not requiring assignments of securities, the office may have limited the availability of deposits to protect the claims of policyholders.

Office personnel are uncertain why the law requires assignment of the deposits. Based on discussion with office personnel and review of supporting documentation, insurance companies place their deposit in trust until the securities mature. At maturity, other qualified securities are exchanged for the mature securities. Office personnel indicated assignment of securities was not continued when companies began exchanging securities.

Findings and Recommendations

Recommendation #3

We recommend the office comply with section 33-2-606, MCA, by obtaining assignment of securities on deposit.

Untimely Deposits

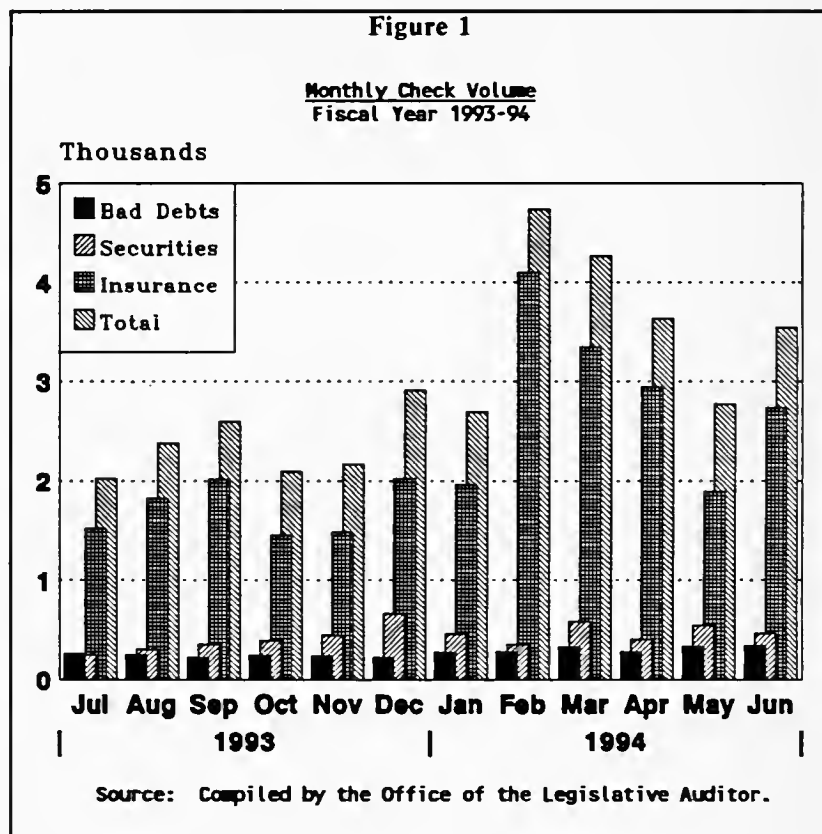
State law requires all revenues received by the office be deposited in the state treasury on a daily basis when the accumulated amount of coin and currency received exceeds \$100 or total receipts exceed \$500. During our audit, we reviewed mail processing and revenue depositing procedures at the office. We noted the following concerns related to the timeliness of deposits.

As part of current procedures, all mail is delivered to the mailroom to be sorted. Once sorted, securities personnel pick up and open securities related mail. Once opened, any checks are returned to the mailroom. All other mail is opened by mailroom personnel. Checks and supporting documentation are separated and placed in the vault until centralized services personnel are available to process the deposit. Through observation we determined the mail is not opened and consequently checks are not processed for deposit on the day received.

To determine the volume of mail processed and percentage that contains checks, we counted mail received for two consecutive days in August 1994. At the time of our count, we identified 362 pieces of unopened mail from the previous business day. We also observed an additional 258 pieces of mail received throughout the day. We determined approximately 30 percent of the total items contained checks totalling \$19,565. We determined deposit of the checks into the state treasury occurred between two to three days after initial receipt. Based on observation and discussion with office personnel, the mailroom routinely has difficulties processing and distributing mail in a timely manner.

Findings and Recommendations

Figure 1 outlines the volume of checks received by the office each month during fiscal year 1993-94. Analysis of this graph indicates August is an average month in terms of the number of checks processed. In addition, we estimated the average number of pieces of mail received per day during fiscal year 1993-94 as 430. The number of items received on each day of our observation was below average. The potential exists for greater delays to occur during months with traditionally high check volume.



Findings and Recommendations

Office personnel indicated two positions are authorized for the mailroom. Mailroom personnel are responsible for both opening mail and processing warrants issued through the warrant writing system. Due to reductions in force and management's decision to meet vacancy savings requirements using the second mailroom position, only one employee is available to perform mailroom duties. The office should review current mail processing procedures and develop alternatives to ensure checks are deposited in accordance with state law.

Recommendation #4

We recommend the office establish mailroom procedures which ensure checks are deposited in accordance with state law.

Unclassified Positions

State law requires all state positions be classified in relation to the state's personnel classification plan. The Department of Administration is responsible for grouping positions into defined classes based on similarity of duties performed, responsibilities assumed, and complexity of work so that similar pay is provided for similar work. State policy prohibits a state agency from appointing a person to any position until that position has been properly classified.

Through review of the office's payroll reports, we determined eight positions were unclassified in addition to the 15 exempt positions reserved for the State Auditor's personal staff. Of the eight positions, five were vacant. At the time of our review the office had not submitted classification requests for these positions, even though the positions were authorized between one and seven years prior to the date of our review. Prior to completion of the audit, the office obtained classification for four of the vacant positions. The office did not obtain classification for the four remaining positions, of which three were filled. By not classifying positions prior to appointing

Findings and Recommendations

individuals to those positions, the office is in noncompliance with state law and policy. Because these positions are unclassified, the office provides compensation based on the budgetary authority provided for each position rather than in relation to the statewide classification plan. The potential exists that the pay provided for these positions is not similar to the pay provided for other positions with similar duties, responsibilities, and complexity of work.

Office personnel agreed the classification of these positions was overlooked but indicated position descriptions are available for the unclassified positions. Office personnel anticipate obtaining classification for the three filled unclassified positions and eliminating the vacant unclassified position.

Recommendation #5

We recommend the office submit classification requests for unclassified positions in a timely manner.

Insurance Examinations

State law requires the office to conduct examinations of domestic insurance companies. During the previous audit, we determined the expenses related to these examinations were not recorded on the state's accounting records. During the current audit we reviewed the status of this prior recommendation and determined the office records the examination activity in the state Special Revenue Fund.

Section 33-1-413, MCA, requires the office to deposit all moneys received for insurance examinations in the General Fund. By recording the examination activity in the Special Revenue Fund, the office is not in compliance with state law. Office personnel stated the activity is not recorded in the General Fund because the appropriation authority for performing the examinations was provided in the Special Revenue Fund. We reviewed the appropriations laws for the 1995 Biennium and

Findings and Recommendations

verified the authority was provided in the Special Revenue Fund. The office should seek legislation to either ensure appropriation authority for performing insurance examinations is provided in the General Fund or amend section 33-1-413, MCA, to allow the revenues to be recorded in the Special Revenue Fund.

Recommendation #6

We recommend the office:

- A. Seek legislation to allow deposit of insurance examination revenues in the Special Revenue Fund, or**
- B. Request General Fund budget authority to spend insurance examination revenues.**

Findings and Recommendations

Reinsurance Board On or Off Book

The office requested us to review whether the Reinsurance Board, created by section 30, Chapter 606, Laws of 1993, is a state program or a nonprofit nonstate entity. The issue concerns whether the program should be on the state's accounting system and subject to legislative appropriation, or "off book" and "off budget."

Chapter 606 relates to universal health care access. In section 30, the legislation created the Montana small employer health reinsurance program administered by a board appointed by the state insurance commissioner. The provisions of section 30 are codified as Sections 33-22-1818 and 33-22-1819, MCA. The question involves whether this program should be treated as a state agency, subject to general laws relating to accounting, budgeting, personnel, audit, etc., or a private nonprofit entity. The answer is unclear based on current law. A review of legislative committee hearing minutes shows no references to the reinsurance program.

The program was created by the legislature and can be modified or abolished by the legislature. The state insurance commissioner appoints the board, approves the operating plan and is required to evaluate the program and file a report annually. These factors would indicate that the program is a state program subject to the general laws applicable to all state agencies.

However, Section 33-22-1818, MCA, provides in part:

"(1) There is a nonprofit entity to be known as the Montana small employer health reinsurance program."

The legislature did not denominate the program as a state program or state agency, but rather a "nonprofit entity."

Section 33-22-1819, MCA, provides in part:

Findings and Recommendations

"(4) The program has the general powers and authority granted under the laws of this state to insurance companies and health maintenance organizations. . .

(11) The program is exempt from taxation."

By giving the program the general powers and duties of an insurance company the legislature is treating the program as a private insurance carrier. The fact the legislature exempted the program from taxation indicates the legislature believed the program could be taxed as a private insurance carrier without the exemption. These factors would indicate the program should be considered a "nonstate" entity.

Under these circumstances, it appears that legislation should be enacted to clarify whether this program is to be administered as a state agency subject to the general laws applicable to state agencies, or administered as a private entity similar to insurance carriers.

Recommendation #7

We recommend the office seek legislation to clarify whether the Reinsurance Board is a state program or a nonprofit nonstate entity.

Independent Auditor's Report & Agency Financial Schedules

Summary of Independent Auditor's Report

Summary of Independent Auditor's Report

The auditor's opinion issued in this report is intended to convey to the reader of the financial schedules the degree of reliance which can be placed on the amounts presented. We included paragraph four in the Independent Auditor's Report to qualify our opinion because the office did not record the effect of refunds payable in the General Fund at fiscal year-end 1992-93 and 1993-94 as described on pages 6 and 7 of this report. The reader should use caution when using the financial information on this schedule.



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Operations and EDP Audit

JAMES GILLETT
Financial-Compliance Audit

JIM PELLEGRINI
Performance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying financial schedules of the State Auditor's Office for each of the two fiscal years ended June 30, 1993 and 1994, as shown on pages A-5 through A-12. The information contained in these schedules is the responsibility of the State Auditor's Office management. Our responsibility is to express an opinion on these financial schedules based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 1, these financial schedules are presented on a comprehensive basis of accounting other than generally accepted accounting principles. The schedules are not intended to be a complete presentation and disclosure of the office's assets and liabilities.

Because the State Auditor's Office did not record the effect of insurance premium tax refunds payable on General Fund revenues, fiscal year 1992-93 revenue, prior year revenue, and support to state of Montana are understated by \$228,184, \$511,872, and \$740,056, respectively. In addition, fiscal year 1993-94 revenue and support to state of Montana are overstated by \$1,935,743 and \$1,124,353 respectively, and prior year revenue is understated by \$811,390.

In our opinion, except for the effects of not recording a liability for estimated premium tax refunds as discussed in the preceding paragraph, the financial schedules referred to in the first paragraph present fairly in all material respects, the results of operations and changes in fund balances of the State Auditor's Office for the two fiscal years ended June 30, 1994, in conformity with the basis of accounting described in note 1.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "James Gillett".

James Gillett, CPA
Deputy Legislative Auditor

August 24, 1994

STATE AUDITOR'S OFFICE
SCHEDULE OF CHANGES IN FUND BALANCES
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1994

	<u>General Fund</u>	<u>Special Revenue Funds</u>	<u>Internal Service Fund</u>
FUND BALANCE: July 1, 1992	\$ <u>0</u>	\$ <u>(124,880)</u>	\$ <u>31,889</u>
ADDITIONS			
<u>Fiscal Year 1992-93</u>			
Budgeted Revenue & Transfers In	26,976,711	20,514,234	142,457
<u>Fiscal Year 1993-94</u>			
Budgeted Revenue & Transfers In	26,028,140	25,590,751	233,214
Cash Transfers In		87,938	
Prior Year Revenue Adjustments		5,545	
Total Additions	<u>53,004,851</u>	<u>46,198,468</u>	<u>375,671</u>
REDUCTIONS			
<u>Fiscal Year 1992-93</u>			
Budgeted Expenditures & Transfers Out	2,365,444	20,607,666	169,118
Prior Year Expenditure Adjustments	6,787	7,772	1,550
Prior Year Revenue Adjustments	890,813 ²		
Direct Entries to Fund Balance	1,259,954 ³		
Support to State of Montana	22,453,713		
Nonbudgeted Expenditures & Transfers Out			879
<u>Fiscal Year 1993-94</u>			
Budgeted Expenditures & Transfers Out	2,073,290	23,786,352	183,873
Prior Year Expenditure Adjustments	88		
Prior Year Revenue Adjustments	740,915 ²		
Support to State of Montana	23,217,827		
Direct Entries to Fund Balance	(3,980)	1,160,334 ¹	324
Nonbudgeted Expenditures & Transfers Out			2,596
Total Reductions	<u>53,004,851</u>	<u>45,562,124</u>	<u>358,340</u>
FUND BALANCE: June 30, 1994	\$ <u>0</u>	\$ <u>511,464</u>	\$ <u>49,220</u>

- ¹ See note 9 on page A-12.
² See note 6 on page A-11.
³ See note 10 on page A-12.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-9.

STATE AUDITOR'S OFFICE
SCHEDULE OF BUDGETED REVENUE & TRANSFERS IN - ESTIMATE & ACTUAL
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1994

	<u>Licenses and Permits</u>	<u>Taxes</u>	<u>Fines & Forfeits</u>	<u>Charges for Services</u>	<u>Investment Earnings</u>	<u>Federal</u>	<u>Total</u>
<u>Fiscal Year 1993-94</u>							
GENERAL FUND							
Estimated Revenue	\$4,060,300	\$19,044,100	\$150,000				\$23,254,400
Actual Revenue	<u>5,348,487</u>	<u>20,162,249</u>	<u>517,404</u>				<u>26,028,140</u>
Collections Over (Under) Estimate	<u>\$1,288,187</u>	<u>\$ 1,118,149</u>	<u>\$367,404</u>				<u>\$ 2,773,740</u>
SPECIAL REVENUE FUNDS							
Estimated Revenue	\$ 563,650 ¹	\$ 8,500,000	\$ 10,000 ¹	\$529,076	\$ 108,000	\$14,000,000	\$23,710,726
Actual Revenue	<u>1,494,963</u>	<u>9,599,839</u>	<u>2,770</u>	<u>532,389</u>	<u>105,886</u>	<u>13,854,904</u> ²	<u>25,590,751</u>
Collections Over (Under) Estimate	<u>\$ 931,313</u>	<u>\$ 1,099,839</u>	<u>\$ (7,230)</u>	<u>\$ 3,313</u>	<u>\$ (2,114)</u>	<u>\$ (145,096)</u>	<u>\$ 1,880,025</u>
INTERNAL SERVICE FUND							
Estimated Revenue				\$194,438			\$ 194,438
Actual Revenue				<u>233,214</u>			<u>233,214</u>
Collections Over (Under) Estimate				<u>\$ 38,776</u>			<u>\$ 38,776</u>
<u>Fiscal Year 1992-93</u>							
GENERAL FUND							
Estimated Revenue	\$3,640,335	\$17,028,000	\$55,000				\$20,723,335
Actual Revenue	<u>4,389,481</u>	<u>22,502,193</u>	<u>85,037</u>				<u>26,976,711</u>
Collections Over (Under) Estimate	<u>\$ 749,146</u>	<u>\$ 5,474,193</u>	<u>\$30,037</u>				<u>\$ 6,253,376</u>
SPECIAL REVENUE FUNDS							
Estimated Revenue	\$ 41,850 ¹	\$ 7,820,000		\$517,358	\$ 185,000	\$10,000,000	\$18,564,208
Actual Revenue	<u>50,316</u>	<u>8,022,211</u>		<u>518,864</u>	<u>83,353</u>	<u>11,839,490</u> ²	<u>20,514,234</u>
Collections Over (Under) Estimate	<u>\$ 8,466</u>	<u>\$ 202,211</u>		<u>\$ 1,506</u>	<u>\$ (101,647)</u>	<u>\$ 1,839,490</u>	<u>\$ 1,950,026</u>
INTERNAL SERVICE FUND							
Estimated Revenue				\$150,817			\$ 150,817
Actual Revenue				<u>142,457</u>			<u>142,457</u>
Collections Over (Under) Estimate				<u>\$ (8,360)</u>			<u>\$ (8,360)</u>

¹ See note 9 on page A-12.

² See note 7 on page A-12.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-9.

STATE AUDITORS OFFICE
SCHEDULE OF BUDGETED PROGRAM EXPENDITURES BY OBJECT & FUND
BUDGET & ACTUAL
FOR THE FISCAL YEAR ENDED JUNE 30, 1994

	State Auditor's Office	Insurance	Securities	Local Assistance Distribution ¹	Forest Res & FPGA To Counties ²	Pension Adj Retired Firemen ¹	Fiscal Control and Management	Total
PERSONAL SERVICES								
Salaries	\$216,765	\$ 874,530	\$ 256,299				\$ 260,211	\$ 1,607,805
Employee Benefits	58,005	219,366	62,483				73,786	413,640
Total	<u>274,770</u>	<u>1,093,896</u>	<u>318,782</u>				<u>333,997</u>	<u>2,021,445</u>
OPERATING EXPENSES								
Other Services	8,943	166,905	8,502				188,472	372,822
Supplies & Materials	10,536	74,832	36,805				16,448	138,621
Communications	9,227	70,380	14,206				301,512	395,325
Travel	1,353	65,096	9,471				791	76,711
Rent	8,230	31,816	8,280				13,521	61,847
Repair & Maintenance	638	3,200	1,100				24,932	29,870
Other Expenses	2,243	24,843	5,620				1,928	34,634
Total	<u>41,170</u>	<u>437,072</u>	<u>83,984</u>				<u>547,604</u>	<u>1,109,830</u>
EQUIPMENT AND INTANGIBLE ASSETS								
Equipment	2,846	7,856	3,906				18,288	32,896
Total	<u>2,846</u>	<u>7,856</u>	<u>3,906</u>				<u>18,288</u>	<u>32,896</u>
LOCAL ASSISTANCE								
From Federal Sources				\$ 0	\$ 13,960,789	\$ 0		13,960,789
From Other Income Sources				7,854,432	0	1,064,123		8,918,555
Total				<u>7,854,432</u>	<u>13,960,789</u>	<u>1,064,123</u>		<u>22,879,344</u>
TOTAL PROGRAM EXPENDITURES	<u>\$318,786</u>	<u>\$1,538,824</u>	<u>\$ 406,672</u>	<u>\$ 7,854,432</u>	<u>\$ 13,960,789</u>	<u>\$ 1,064,123</u>	<u>\$ 899,889</u>	<u>\$26,043,515</u>
GENERAL FUND								
Budgeted	\$314,730	\$1,248,266	\$ 340,266				\$ 218,936	\$ 2,122,198
Actual	308,366	1,223,790	331,852				209,282	2,073,290
Unspent Budget Authority	<u>\$ 6,364</u>	<u>\$ 24,476</u>	<u>\$ 8,414</u>				<u>\$ 9,654</u>	<u>\$ 48,908</u>
SPECIAL REVENUE FUNDS								
Budgeted	\$ 13,467	\$ 535,022	\$ 75,500 ³	\$ 7,950,000	\$ 15,000,000	\$ 1,150,000	\$ 525,902	\$25,249,891
Actual	3,485	315,034	74,820 ³	7,854,432	13,960,789	1,064,123	513,669	23,786,352
Unspent Budget Authority	<u>\$ 9,982</u>	<u>\$ 219,988</u>	<u>\$ 680</u>	<u>\$ 95,568</u>	<u>\$ 1,039,211</u>	<u>\$ 85,877</u>	<u>\$ 12,233</u>	<u>\$ 1,463,539</u>
INTERNAL SERVICE FUND								
Budgeted	\$ 6,935						\$ 188,800	\$ 195,735
Actual	6,935						176,938	183,873
Unspent Budget Authority	<u>\$ 0</u>						<u>\$ 11,862</u>	<u>\$ 11,862</u>

- ¹ See note 5 on page A-11
² See note 7 on page A-11
³ See note 9 on page A-12

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-9.

STATE AUDITOR'S OFFICE
SCHEDULE OF BUDGETED PROGRAM EXPENDITURES BY OBJECT & FUND
BUDGET & ACTUAL
FOR THE FISCAL YEAR ENDED JUNE 30, 1993

	State Auditor's Office	State Payroll ¹	Insurance	Securities	Local Assistance Distribution ²	Forest Res & FPGA To Counties ³	Pension Adj Retired Firemen ²	Fiscal Control and Management	Total
PERSONAL SERVICES									
Salaries	\$182,742	\$191,389	\$678,926	\$ 230,064				\$247,911	\$ 1,531,032
Employee Benefits	43,498	46,163	160,102	52,562				64,943	367,268
Total	<u>226,240</u>	<u>237,552</u>	<u>839,028</u>	<u>282,626</u>				<u>312,854</u>	<u>1,898,300</u>
OPERATING EXPENSES									
Other Services	10,539	329,859	51,119	47,366				223,136	662,019
Supplies & Materials	33,292	2,330	10,997	6,513				3,710	56,842
Communications	6,610	8,823	43,463	10,644				285,818	355,358
Travel	3,192	212	19,871	3,990				154	27,419
Rent	2,713	16,276	18,533	3,373				16,276	57,171
Repair & Maintenance	593	1,765	1,748	522				15,480	20,108
Other Expenses	958	1,452	9,553	1,838				488	14,289
Total	<u>57,897</u>	<u>360,717</u>	<u>155,284</u>	<u>74,246</u>				<u>545,062</u>	<u>1,193,206</u>
EQUIPMENT AND INTANGIBLE ASSETS									
Equipment	4,367							6,751	11,118
Total	<u>4,367</u>							<u>6,751</u>	<u>11,118</u>
LOCAL ASSISTANCE									
From Federal Sources						\$11,918,322			11,918,322
From Other Income Sources					\$7,079,021		\$1,042,261		8,121,282
Total					<u>7,079,021</u>	<u>11,918,322</u>	<u>1,042,261</u>		<u>20,039,604</u>
TOTAL PROGRAM EXPENDITURES	<u>\$288,504</u>	<u>\$598,269</u>	<u>\$994,312</u>	<u>\$356,872</u>	<u>\$7,079,021</u>	<u>\$11,918,322</u>	<u>\$1,042,261</u>	<u>\$864,667</u>	<u>\$23,142,228</u>
GENERAL FUND									
Budgeted	\$290,602	\$223,446	\$958,357	\$363,384				\$551,089	\$ 2,386,878
Actual	<u>288,504</u>	<u>218,886</u>	<u>952,465</u>	<u>356,872</u>				<u>548,717</u>	<u>2,365,444</u>
Unspent Budget Authority	<u>\$ 2,098</u>	<u>\$ 4,560</u>	<u>5,892</u>	<u>\$ 6,512</u>				<u>\$ 2,372</u>	<u>\$ 21,434</u>
SPECIAL REVENUE FUNDS									
Budgeted		\$435,526	\$ 41,850		\$7,500,000	\$14,000,000	\$1,050,000	\$ 146,832	\$23,174,208
Actual		<u>379,383</u>	<u>41,847</u>		<u>7,079,021</u>	<u>11,918,322</u>	<u>1,042,261</u>	<u>146,832</u>	<u>20,607,666</u>
Unspent Budget Authority		<u>\$ 56,143</u>	<u>\$ 3</u>		<u>\$ 420,979</u>	<u>\$ 2,081,678</u>	<u>\$ 7,739</u>	<u>\$ 0</u>	<u>\$ 2,566,542</u>
INTERNAL SERVICE FUND									
Budgeted								\$ 195,661	\$ 195,661
Actual								<u>169,118</u>	<u>169,118</u>
Unspent Budget Authority								<u>\$ 26,543</u>	<u>\$ 26,543</u>

- ¹ See note 8 on page A-12.
² See note 5 on page A-11.
³ See note 7 on page A-11.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-9.

Notes to the Financial Schedules

For the Two Fiscal Years Ended June 30, 1994

1. Summary of Significant Accounting Policies

Basis of Accounting

The office uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental Funds. In applying the modified accrual basis, the office records:

Revenues when it receives cash or when receipts are measurable and available to pay current period liabilities.

Expenditures for valid obligations when the office incurs the related liability and it is measurable.

State accounting policy also requires the office to record the cost of employees' annual leave and sick leave when used or paid.

The office uses accrual basis accounting for its Proprietary Fund. Under the accrual basis, as defined by state accounting policy, the office records revenues in the accounting period earned if measurable and records expenses in the period incurred, if measurable.

Expenditures and expenses may include: entire budgeted service contracts even though the office received the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

Basis of Presentation

The financial schedule format is in accordance with the policy of the Legislative Audit Committee. The financial schedules are prepared from the Statewide Budgeting and Accounting System without adjustment. Accounts are organized in funds according to state law. The office uses the following funds:

Governmental Funds

General Fund - to account for all financial resources except those required to be accounted for in another fund. The following divisions are funded in part by General Fund moneys: Central Administration; Insurance; Securities; and Fiscal

Notes to the Financial Schedules

Control & Management, which includes the Warrant Writer function. In Fiscal Year 1992-93, there was a direct appropriation from the General Fund for payroll services to General Fund employees.

Special Revenue Fund - to account for proceeds of specific revenue sources legally restricted to expenditures for specific purposes. Office Special Revenue Funds include certain Insurance and Securities Division activity. This includes the Firemen's and Municipal Police Officer's Pension Tax, Fire Prevention & Investigation Tax, Insurance Industry Continuing Education Program, and Securities Portfolio Registration Program. The office also records the receipt and distribution of Federal Forest Reserve Funds to counties within Montana in the Special Revenue Fund.

Proprietary Fund

Internal Service Fund - to account for providing goods or services to other agencies or departments on a cost-reimbursement basis. The office Internal Service Fund accounts for the Bad Debts Collection System, which retains a percentage of the bad debt collections made on behalf of state agencies.

2. Annual and Sick Leave

Employees at the office accumulate both annual and sick leave. The office pays employees for 100 percent of unused annual and 25 percent of unused sick leave credits upon termination. Accumulated unpaid liabilities for annual and sick leave are not reflected in accompanying financial schedules. In the Proprietary Funds, the increase in annual and 25 percent of the increase in sick leave are recognized as nonbudgeted expenses when the related liability is recorded at year end. The office absorbs expenditures for termination pay in its annual operational costs. At June 30, 1992-93 and at June 30, 1993-94, the office had a liability of \$123,489 and \$162,740, respectively.

3. Pension Plan

Employees are covered by the Montana Public Employees' Retirement System (PERS). The office's contribution to PERS was \$98,218 in fiscal year 1992-93 and \$107,470 in fiscal year 1993-94.

4. General Fund Balance

The General Fund is a statewide fund. Agencies do not have a separate General Fund since their only authority is to pay obligations from the statewide General Fund within their appropriation limits. Thus, on an agency's schedules, the General Fund beginning and ending fund balance will always be zero.

5. Local Assistance Distributions

In accordance with state law the office collects Fire Prevention & Investigation, Fireman's Pension, and Premium Taxes on insurance premiums written in the state of Montana. The Fire Prevention & Investigation Tax is distributed to cities and towns within Montana having a fire department relief association. The moneys are intended for the benefit and use of the association. The Firemen's Pension Tax is also distributed to cities and towns having fire department relief associations. This tax is used to finance pension payments made to retired firefighters. A portion of the Premium Tax is used to fund the Municipal Police Officers Retirement System.

The above described distributions are recorded as Local Assistance Distributions on the Schedule of Budgeted Program Expenditures by Object and Fund. The Firemen's Pension Tax distribution amounted to \$1,042,261 in Fiscal Year 1992-93 and \$1,064,123 in Fiscal Year 1993-94. The distribution for the Fire Prevention and Investigation Tax and the Municipal Police Officers Retirement System totalled \$7,079,021 and \$7,854,432 in fiscal years 1992-93 and 1993-94, respectively.

6. Premium Tax Refunds

The office processed premium tax refunds worth \$511,872 and \$811,390 in Fiscal Years 1992-93 and 1993-94, respectively, to insurance companies having large credit balances. These refunds represent the majority of the Prior Year Revenue Adjustments on the Schedule of Changes in Fund Balance for the Two Fiscal Years Ended June 30, 1994.

7. Federal Forest Reserve Funds

The office receives Federal Forest Reserve Funds from the U.S. Department of Agriculture. This revenue is derived from timber sales, grazing fees, land use fees, recreation charges, utility fees,

Notes to the Financial Schedules

mineral revenues, and admission and user fees related to National Forest land located in Montana. The office distributes these funds plus the related investment earnings to counties in accordance with the requirements of section 17-3-212, MCA. The distribution totalled \$11,918,322 and \$13,960,789 in Fiscal Years 1992-93 and 1993-94, respectively.

8. State Payroll

The 1993 Legislature transferred the State Payroll program to the Department of Administration effective July 1, 1993. The transfer reduced office personal service and operating expenses by approximately \$450,000 in Fiscal Year 1993-94.

9. Portfolio Registration Fee

The office implemented the Portfolio Registration program on October 1, 1993. Total revenue received in fiscal year 1993-94 from this program was \$1,099,555. In accordance with section 30-10-115, MCA, the office transferred the program's fund balance to the General Fund. The transfer appears on the Schedule of Changes in Fund Balance for the Two Fiscal Years ended June 30, 1994 as a reduction of \$1,160,334 in the Special Revenue Fund recorded as a direct entry to fund balance. Due to human error, the deposit exceeded the program's available fund balance by \$135,599. Office personnel identified and corrected the error in Fiscal Year 1994-95. The deposit will also appear as an addition to the General Fund on the Department of Administration financial schedules, recorded as a direct entry to fund balance.

10. Municipal Police Officer's Retirement System Payment

In fiscal year 1992-93 the Public Employees' Retirement Division requested the office to submit a payment to the Municipal Police Officer's Retirement System for fiscal years 1985-86 through 1992-93. The office recorded a direct entry to fund balance in the General Fund of \$1,267,498 for the contribution relating to fiscal years 1985-86 through 1990-91. The fiscal year 1991-92 and 1992-93 amounts of \$357,601 and \$363,035 were recorded as prior year and current year activity, respectively.

Agency Response

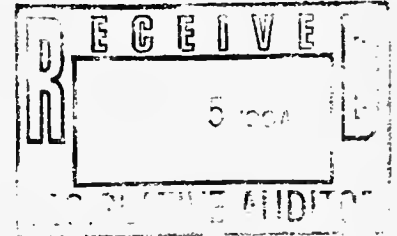
STATE AUDITOR
STATE OF MONTANA

Mark O'Keefe
STATE AUDITOR



COMMISSIONER OF INSURANCE
COMMISSIONER OF SECURITIES

November 14, 1994



Mr. Scott A. Seacat, Legislative Auditor
Office of the Legislative Auditor
State Capitol
PO Box 201705
Helena, MT 59620-1705

Dear Mr. Seacat:

We have reviewed your financial compliance audit for the two fiscal years ended June 30, 1994. Our response to each audit recommendation follows:

Recommendation #1

We recommend the office establish procedures to properly authorize, test, and document programming changes to facilitate recording revenue on SBAS in accordance with state accounting policy.

Agency Response:

We concur. All subsequent programming changes have been documented and tested according to state data processing policy. The receipting system now provides accurate data for recording revenue on SBAS. All future modifications will be tested and documented to assure compliance with data processing policy.

Recommendation #2

We recommend the office establish procedures to estimate and annually record premium tax refunds payable.

Agency Response:

We concur. Premium tax refund liability has not been recorded since FY88 when it became a liability issue due to quarterly estimated payments. We will establish procedures to correctly record premium tax refunds payable for FY 1995.

Recommendation #3

We recommend the office comply with section 33-2-606, MCA, by obtaining assignment of securities on deposit.

Agency Response:

We concur. In the early 80's, the State Auditor adopted the current process for assignments. We have initiated the correct procedure to comply with this audit recommendation.

Recommendation #4

We recommend the office establish mailroom procedures which ensure checks are deposited in accordance with state law.

Agency Response:

We concur. The mail room is currently fully staffed. A reduction in force occurred in January of 1993 and reduced our supplemental request to the 93 session by \$7,500 in General Fund. We will attempt to maintain staffing to insure prompt deposit of incoming checks. We will review our receipting process to determine if a more efficient method can be developed to expedite deposit and maintain proper security and documentation.

Recommendation #5

We recommend the office submit classification requests for unclassified positions in a timely manner.

Agency Response:

We concur. We will expedite the final classification of a data processing position and two actuary positions.

Recommendation #6

We recommend the office:

- A. Seek legislation to allow deposit of insurance examination revenues in the Special Revenue Fund, or**
- B. Request General Fund budget authority to spend insurance examination revenues.**

Mr. Scott A. Seacat, Legislative Auditor
Page 3
November 14, 1994

Agency Response:

We concur. Until FY94, these costs were not recorded on the state accounting system. We requested and received legislative authority to record these costs under the state special revenue fund. We plan to seek legislation allowing us to continue this practice in the 1995 Legislative Session.

Recommendation #7

We recommend the office seek legislation to clarify whether the Reinsurance Board is a state program or a nonprofit nonstate entity.

Agency Response:

We concur. We believe the Reinsurance Board should be a nonprofit, nonstate entity. We will seek legislation in the 95 Session clarifying this position.

I would like to thank your staff for their time and effort during this audit. They were very helpful addressing issues that concerned my staff and pointing out areas that need improvement.

Sincerely,



Mark O'Keefe
State Auditor

MO/tcp

